

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

Chrono
SPECIAL

LEGISLATIVE REFERRAL MEMORANDUM

TO: LEGISLATIVE LIAISON OFFICER

Department of Agriculture
Central Intelligence Agency ✓
Department of Commerce
Department of Defense
Department of Education
Department of Energy
Environmental Protection Agency
Federal Emergency Management Agency
General Services Administration
Administrative Office of the U.S. Courts
Department of Health and Human Services
Department of Housing and Urban Development

Department of the Interior
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Department of Transportation
Department of the Treasury
Veterans Administration
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United States Postal Service
Small Business Administration
National Aeronautics and Space Administration

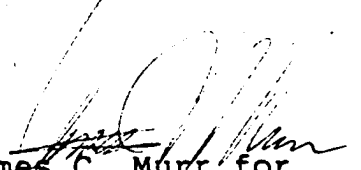
SUBJECT: H.R. 3689, H.R. 3690, H.R. 3691, H.R. 3692, H.R. 3693 and draft DOJ report on the preceding bills related to restricting or abolishing Federal diversity jurisdiction

The Office of Management and Budget requests the views of your agency on the above subject before advising on its relationship to the program of the President, in accordance with OMB Circular A-19.

Please provide us with your views no later than

Friday, May 4, 1984.

Direct your questions to Branden Blum (395-3802), the legislative attorney in this office.


James C. Murr for
Assistant Director for
Legislative Reference

Enclosure

cc: K. Wilson
F. Fielding

M. Uhlmann
M. Horowitz

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Office of Legislative Affairs

Office of the Assistant Attorney General

Washington, D.C. 20530

Honorable Robert W. Kastenmeier
Chairman
Subcommittee on Courts, Civil Liberties,
and the Administration of Justice
Committee on the Judiciary
House of Representatives
Washington, D. C. 20515

Dear Chairman Kastenmeier:

This is in response to your request for the views of the Department of Justice on H.R. 3689, 3690, 3691, 3692, and 3693, bills relating to the diversity jurisdiction of the federal courts. H.R. 3689 proposes the complete abolition of federal jurisdiction based on diversity of state citizenship, except for statutory interpleader; the remaining bills set out intermediate reform options. The Department of Justice supports the enactment of the complete abolition proposal of H.R. 3689 without qualification. We would also support the enactment of the general types of reforms proposed in the other bills as preferable alternatives to the current system.

Our views concerning the grounds for abolishing diversity jurisdiction -- or limiting it as far as possible if complete abolition cannot be achieved -- have been stated in previous submissions to this Subcommittee. ^{1/} This report will accordingly be concerned, for the most part, with an analysis of the design and probable effects of the various reform options. A final section sets out some additional options that merit consideration by the Subcommittee.

^{1/} See Diversity of Citizenship Jurisdiction - 1982: Hearing on H.R. 6691 Before the Subcomm. on Courts, Civil Liberties and the Administration of Justice of the House Comm. on the Judiciary, 97th Cong., 2d Sess. 7-16 (1982) (testimony and supplementary submission of Assistant Attorney General Jonathan C. Rose) [hereafter cited as "1982 House Diversity Jurisdiction Hearing"].

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I. H.R. 3689 -- The "Complete Abolition" Proposal

H.R. 3689 would generally abolish the diversity jurisdiction of the federal courts. The grounds for this reform have been discussed in our earlier statements and in the voluminous hearings on diversity jurisdiction reform that have been held in both Houses of Congress over the past six years. 2/

H.R. 3689, like earlier "complete abolition" proposals, would retain statutory interpleader. In contrast to the general diversity jurisdiction of the federal courts, the interpleader action serves a valid purpose. It permits a dispositive adjudication of liability with respect to a fund where multiple liability might otherwise result from inconsistent verdicts in proceedings in different states. 3/

H.R. 3689 differs from earlier "complete abolition" bills in providing that its elimination of diversity jurisdiction is to lapse after five years. This provision is not intrinsically desirable, since it risks a repetition a few years from now of

2/ See id.; Diversity of Citizenship Jurisdiction/Magistrates Reform - 1979: Hearings on H.R. 1046 and H.R. 2202 Before the Subcomm. on Courts, Civil Liberties and the Administration of Justice of the House Comm. on the Judiciary, 96th Cong., 1st Sess. (1979) [hereafter cited as "1979 House Diversity Jurisdiction Hearings"]; Jurisdictional Amendments Act of 1979, S. 679: Hearings Before the Senate Comm. on the Judiciary, 96th Cong., 1st Sess. (1979) [hereafter cited as "1979 Senate Diversity Jurisdiction Hearings"]; Federal Diversity of Citizenship Jurisdiction: Hearings on S. 2094, S. 2389 and H.R. 9622 Before the Subcomm. on Improvements in Judicial Machinery of the Senate Comm. on the Judiciary, 95th Cong., 2d Sess. (1978) [hereafter cited as "1978 Senate Diversity Jurisdiction Hearings"]; Diversity of Citizenship Jurisdiction/Magistrates Reform: Hearings Before the Subcomm. on Courts, Civil Liberties and the Administration of Justice of the House Comm. on the Judiciary, 95th Cong., 1st Sess. (1977) [hereafter cited as "1977 House Diversity Jurisdiction Hearings"].

3/ Outside of interpleader cases, diversity jurisdiction does not generally promote the efficient and consistent adjudication of related cases; it can easily have the opposite effect. Specifically, cases which would have been handled as consolidated proceedings in state court may be split into separate state and federal proceedings when some parties choose to litigate in federal court and other parties must stay in state court because they lack the requisite diversity of citizenship.

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the battle over diversity reform. It would be justified only as a pragmatic concession, if such a concession is needed to gain acceptance of the proposal.

II. H.R. 3690 -- Abolition of General Diversity Jurisdiction And Creation of a Mass Tort Action

H.R. 3690 would abolish the general diversity jurisdiction of the federal courts in the same manner as H.R. 3689 and would provide a federal forum for certain multiparty or mass tort cases on the basis of minimum diversity.

We have previously stated support for the creation of this type of multiparty action. 4/ As an isolated measure, this proposal might be criticized as adding to the workload of a judicial system that is already heavily overloaded. However, this objection has little force against the adoption of the proposal as an element in a broader program of diversity jurisdiction reduction. The savings from H.R. 3690's general abolition of diversity jurisdiction, in particular, would vastly exceed any additional work resulting from the creation of a properly designed multiparty action. 5/

The proposed action would provide a more efficient means of adjudicating mass disaster or mass tort cases, such as those arising from airplane crashes. The existing diversity jurisdiction of the federal courts does not ensure that a consolidated forum will be available in such cases, since the multiplicity of parties makes it likely that some of the parties will lack the required diversity of citizenship. 6/ The proposed multiparty action based on minimum diversity avoids this problem. 7/ As a

4/ See 1982 House Diversity Jurisdiction Hearing, supra note 1, at 11-13, 15-16.

5/ Diversity cases account for about one quarter of all civil filings, 40% of all civil trials, and 60% of all civil jury trials in the federal district courts.

6/ See, e.g., Air Disaster Litigation: Hearings on H.R. 1027 Before the Subcomm. on Administrative Law and Governmental Relations of the House Comm. on the Judiciary, 97th Cong., 1st & 2d Sess. 43-44 (1982) (110 unresolved cases arising from plane crash remained in state court on account of lack of diversity) [hereafter cited as "Air Disaster Litigation Hearings"].

7/ The proposal of H.R. 3690 also avoids the limitation of the general authority of the Panel on Multidistrict Litigation to consolidation of proceedings for pre-trial purposes. The
(Footnote Continued)

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practical matter, the creation of this action offers an advantage to some potential litigants that may help offset resistance to diversity reform.

The formulation of the multiparty action contained in H.R. 3690 was initially proposed by the Department of Justice in 1979. 8/ It is generally well designed to achieve its purposes. A federal forum would be available on the basis of minimum diversity 9/ where at least twenty-five people have each incurred injury to their persons or property exceeding \$10,000 as the result of a "single event, transaction, occurrence, or course of conduct." 10/ Once such an action had been commenced in federal

(Footnote Continued)

court to which cases are transferred for consolidated pre-trial proceedings may, as a practical matter, sometimes retain them for trial as well, but this possibility is limited by venue rules. See 1979 House Diversity Jurisdiction Hearings, supra note 2, at 161.

8/ See id. at 158-62.

9/ Both the original version of the proposal and H.R. 3690 add some limited requirements to the minimum diversity standard, so as to exclude cases of a "purely local" nature. See id. at 160. The original proposal limited the action to cases in which (i) minimum diversity between adverse parties exists and in addition a plaintiff and some other injured party are citizens of different states, or (ii) a party is a state citizen and an adverse party is a foreign state or a citizen of a foreign state. This bill adds a third clause covering cases in which minimum diversity between adverse parties exists and in addition at least two defendants reside in different states. In the formulation of this new clause it would be preferable to use the notion of "citizenship" instead of "residence," since these concepts are not technically the same and the notion of "residence" might be unclear as applied to corporations.

10/ The bill differs slightly from the original version of the multiparty action proposed by the Department of Justice, see id. at 158, in requiring a "good faith" allegation concerning these jurisdictional conditions. This is apparently meant to convey that the good faith-legal certainty test that is normally applied to jurisdictional amount claims, see note 27 and accompanying test infra, would also apply in the proposed multiparty action. However, this test is not indicated by explicit language in other jurisdictional amount provisions; the term "good faith" is not a fully satisfactory formulation since the

(Footnote Continued)

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court, other injured parties could intervene as additional plaintiffs, and the defendant could remove to federal court all related cases brought against it in state court.

The Panel on Multidistrict Litigation would be authorized to transfer all of the actions to a single district court (the "transferee court") for consolidated pre-trial proceedings and a consolidated trial on the question of liability. Actions would be remanded to their district courts of origin for separate trials on the question of damages, unless the equities of the case favored having the transferee court make the damage determinations as well. The transferee court would not be bound by normal choice of law rules, but would apply the same substantive law in all actions.

While we generally approve of the design of the proposed action, we have comments on a few points which merit further consideration by the Subcommittee. These are generally directed at minimizing the need for litigation on questions of interpretation; ensuring that the proposed action has a predictable scope; and ensuring that it operates efficiently:

The Definition of Injury. The action would be predicated on "personal injury or injury to the property" of at least twenty-five persons. It would be desirable to clarify in the proposal's legislative history that "personal injury" means physical harm to natural persons (including death) and that "injury to property" means physical damage to, or destruction of, tangible property.

This interpretation is consistent with the natural understanding of the language of the proposal and with the intent suggested by its legislative history. ^{11/} It would foreclose interpretive litigation over the adequacy of intangible "injury" as a basis for jurisdiction under the action, such as the financial loss or harm involved in fraud or breach of contract cases. In terms of policy, there is little justification for extending the scope of the action to such cases. The commercial

(Footnote Continued)

normal standard allows dismissal where it is legally certain that the jurisdictional amount cannot be recovered, even in the absence of subjective bad faith; and the language of the bill appears to apply its "good faith" requirement to the allegation concerning the number of persons injured rather than to the allegation concerning the value of their injuries. It might be preferable to address this question by stating in legislative history that the normal standards for assessing jurisdictional claims would apply, rather than through a formulation incorporated in the language of the bill.

^{11/} See note 12 infra.

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torts that most commonly result in financial harm to a large number of parties in a number of states -- such as antitrust violations and securities frauds -- can already be sued on in federal court on other jurisdictional bases.

Qualifying Events and Occurrences. The proposal refers to injury resulting from a "single event, transaction, occurrence, or course of conduct." It is clear both from the language of the proposal and from its legislative history that the action is meant to apply to mass injury cases arising from discrete, spatially and temporally limited incidents, such as an airplane crash, a train derailment, or a hotel fire. ^{12/} The term "course of conduct," however, creates an ambiguity as to what other classes of cases may also fall within the scope of the action:

Example: In the years following World War II, employees at a shipyard are exposed to asbestos in the course of their work. After a lapse of decades, some of the former employees of the shipyard become sick, which they believe to be the result of their exposure to asbestos. They attempt to bring federal multiparty actions, arguing that the employer's failure to take adequate precautions against asbestos exposure over a period of years constituted "a single...course of conduct."

The number of straightforward mass disaster cases, exemplified by major commercial aviation accidents, is limited;

^{12/} In testimony before the Senate Judiciary Committee in 1979, the Department of Justice stated that the point of a multiparty action of the sort proposed in H.R. 3690 would be to address "mass tort" cases. It was stated that "[t]he most common example is the commercial airline crash; however, there are other types of mass injury cases that would also be affected such as bus or train accidents." See 1979 Senate Diversity Jurisdiction Hearings, supra note 2, at 31-32.

Similarly, in testimony before this Subcommittee explaining the possible desirability of creating a special action for "mass tort" cases, the Department stated that "[a]nother possible situation in which the diversity jurisdiction could serve some genuinely useful purpose today is in so-called 'mass tort' situations. A typical example is an airline crash where dozens or even 200 or 300 persons are injured or killed...." See 1979 House Diversity Jurisdiction Hearings, supra note 2, at 148. The Department's statement accompanying the initial proposal of the multiparty action contained in H.R. 3690 consistently referred to injuries resulting from a single "incident." See id. at 160.

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admitting such cases to the federal courts on a "minimum diversity" basis should result in no excessive burdens for the courts if it is accompanied by the elimination of the general diversity jurisdiction. However, the effect of including a vaguely defined class of mass injury cases arising from more diffuse patterns of actions or occurrences is more difficult to anticipate.

While it is dubious that such cases were meant to be within the scope of the proposed multiparty action, under the current formulation of the proposal a large potential exists for litigation over how far the notion of "a single...course of conduct" can be stretched. As a matter of policy, it is not apparent that a federal judicial remedy designed primarily for aviation disasters and other cases of a similar character would be a suitable or adequate means of dealing with other types of mass injury litigation. 13/

13/ Consider, for example, mass injury cases in which thousands of suits may be commenced against the same defendant over a period of years or decades. Mechanisms may be desired in such cases -- such as permanent compensation funds -- which ensure that earlier litigants do not deplete the assets of the defendant, leaving little or nothing for plaintiffs who discover their injuries and commence litigation at a later time.

The multiparty action proposed in H.R. 3690 makes no provision for the interests of parties who have not commenced litigation at the time the consolidated proceeding is concluded in the transferee court. This omission is not a problem for aviation cases and other mass disaster cases in which the injury is immediately apparent and litigation is generally commenced promptly after the incident. It would have very different implications, however, in connection with asbestos litigation and other litigation of a similar character. See generally The Manville Bankruptcy and the Northern Pipeline Decision: Hearing Before the Subcomm. on Courts of the Senate Comm. on the Judiciary, 97th Cong., 2d Sess. (1982); Court Improvements Act of 1983: Hearings on S. 645 Before the Subcomm. on Courts of the Senate Comm. on the Judiciary, 98th Cong., 1st Sess. 183-84 (1983); Rotbart, Manville Corporation Faces Increasing Opposition to Bankruptcy Filing, Wall St. J., Jan. 31, 1984, at 1.

The simplest response to these problems would be to delete the terms "course of conduct" and "transaction" 14/ from the bill. This would preserve the action for all cases that are clearly within its intended scope -- mass injury actions resulting from a single event or occurrence -- but would foreclose litigation over its possible application in broader areas. Defining the particular action proposed in H.R. 3690 in this manner would not, of course, prevent the Subcommittee from examining the problems of other types of mass injury litigation as a separate undertaking from diversity jurisdiction reform.

Transferable Actions. The bill's provision regarding transfer and consolidation, 28 U.S.C. § 1407(i), refers to transferred actions in which jurisdiction is based on the proposed multiparty action, 28 U.S.C. § 1367. This should be broadened to refer to all actions based on an event or occurrence which provides the jurisdictional basis for a multiparty action. If some suits arising from a mass disaster are brought in federal court under proposed § 1367, while other suits arising from the same incident are brought under other jurisdictional bases, such as the general alienage jurisdiction, 15/ it should still be possible to handle all of the actions under the consolidated procedure proposed in the bill. The bill's current language is not adequate for this purpose.

14/ While the term "course of conduct" carries the greater expansive potential, deletion of the term "transaction" also seems advisable, unless some specific class of cases within the intended scope of the action can be described which would be included if "transaction" were retained and excluded if "transaction" were taken out. In general, it is unclear what "transaction" adds to the unproblematic terms "event" and "occurrence."

15/ H.R. 3690 would retain the general alienage jurisdiction which is currently provided in 28 U.S.C. §1332(a)(2). In a suit qualifying as a multiparty action which involved adverse parties who were American citizens and citizens of foreign states respectively, there would apparently be the option of proceeding under the general alienage jurisdiction provision, or the proposed multiparty action, or both.

There are various other potentially overlapping grounds of federal jurisdiction. For example, the sinking of a ship that gives rise to a multiparty action may also give rise to Jones Act suits, see 46 U.S.C. §688, to Death on the High Seas Act suits, see 46 U.S.C. §§761-68, and to general admiralty jurisdiction suits, see 28 U.S.C. §1333. Aviation disasters often involve claims against the government under the Federal Tort Claims Act. See Douglas, Air Disaster
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Choice of Law. Under currently popular choice of law theories, the law of different jurisdictions may be applied to different parties in the same case on account of differences in their domiciles or other factors. The choice of law may also differ for the various elements in a single party's case. For example, the law of different jurisdictions may be applied in connection with the applicable standard of care and other rules of liability, presumptions and burdens of proof, rules of contributory or comparative negligence, the amounts and types of compensatory damages that may be awarded, the availability of punitive damages, rules governing contribution among joint tortfeasors, and the limitation period applicable to the action.

This fragmentation of the substantive law applied in a case has had unfortunate consequences in mass disaster cases of the sort addressed by H.R. 3690, which involve dozens of parties from a number of states. Specific problems that have arisen include choice of law litigation of staggering complexity 16/; complications in the adjudication of the merits of the case resulting from the need to apply different bodies of law to different parties 17/ and different issues 18/; delay in settlements resulting from uncertainty over which state's law will be applied 19/; the impetus to forum-shopping created by the perception that a particular forum will apply a more or less favorable body of law 20/; and the perceived unfairness of drastically different recoveries 21/ that may result when different bodies of law are applied to different parties in the same case. 22/

(Footnote Continued)

Litigation Without Diversity, 45 J. Air L. & Comm. 411, 438-39 (1980).

16/ See, e.g., In re Air Crash Disaster Near Chicago, 644 F.2d 594 (7th Cir. 1981).

17/ See Air Disaster Litigation Hearings, supra note 6, at 38.

18/ See id. at 77.

19/ See id. at 104-05.

20/ See id. at 106-07.

21/ See id. at 40, 78, 102.

22/ It is not apparent what there is to show for all the time and effort that is expended as a result of choice of law problems in these cases. It is a debatable proposition that the tort law of one state is better or more just than the law of some other state that might be applied, and in any

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H.R. 3690 provides that the transferee court would not be bound by normal choice of law rules, but would apply the same substantive law 23/ in all actions. This would eliminate the application of the law of different jurisdictions to different parties. With appropriate clarification, it would also go far toward eliminating the other problems related to choice of law in mass tort cases. Specifically, it should be made clear that the application of the same substantive law to all actions includes a requirement that the same law generally be applied to all aspects and elements of each party's action, and that the transferee court's choice of law would carry over to the district courts of origin in remands for separate trials on the question of damages. This approach would not avoid the need for a choice of law by the transferee court, but only one choice would be required. Following this choice, the same body of law would be applied uniformly in all subsequent proceedings. 24/

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event few courts employ choice of law rules that make the applicable law depend on such value judgments. There must be some limit on the costs justified by determinations that have nothing to do with the merits of the case and further no interest of justice.

23/ "Substantive law" should be understood in the normal choice-of-law sense. It does not include the choice-of-law rules of the state and does not include matters that are purely procedural, that is, the range of matters governed by the Federal Rules of Civil Procedure and local rules of court in the federal courts.

24/ The suggested principle of uniformity requires some limited qualifications. If a claim or issue is governed by federal law, the transferee court should, of course, apply the pertinent federal law. For example, a multiparty action arising from a train derailment might incorporate Federal Employer's Liability Act (FELA) claims, see 45 U.S.C. §§51-60, and a multiparty action arising from the sinking of a ship might incorporate Jones Act claims, see 46 U.S.C. §688.

Where necessary to avoid unfair surprise, the standards of conduct provided by a state's law should be applied to conduct which does not have a potential impact outside of the state. For example, in a bus accident case, the driver's negligence must obviously be reckoned in light of the speed limit and other rules of the road of the place in which he was driving, even if some other state's law is generally applied in the case. See Reese, Depecage: A Common Phenomenon in Choice of Law, 73 Colum. L. Rev. 58, 63-64 (1973). On the other hand, there would be no unfairness in applying the law of the state chosen,

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As an alternative to providing for the uniform application of the law of a single, unspecified jurisdiction in all actions -- the approach of the current formulation of the bill -- the Subcommittee might consider the possibility of including an explicit choice of law rule in the bill. The bill could, for example, state a general rule that the substantive law of the state in which the transferee court is located is to be applied.^{25/} This would provide uniformity and optimal simplicity in the choice of law, and would utilize the body of state law with which the judge of the transferee court is most likely to be familiar. The Panel on Multidistrict Litigation would be required, in any event, to make a decision concerning the district in which the actions are to be consolidated. Many

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whichever it might be, in reckoning the liability of a manufacturer for a defective part incorporated into an airplane which may be flown in other states.

It may also be desirable to state some qualification to ensure that the normal operation of state workmen's compensation systems -- and other state compulsory insurance systems adopted as a replacement for litigation -- will not be interfered with, where the state whose law is generally applied in the case is not the state which administers the applicable compensation system. Cf. 28 U.S.C. § 1445(c) (civil action in state court arising under state's workmen's compensation laws not removable to federal court).

While this question merits consideration by the Subcommittee, it would appear that applying the same state's law to all issues would rarely present any problem in connection with the issues that are likely to pose significant choice of law questions in mass tort cases. See generally Air Disaster Litigation Hearings, supra note 7, at 75-78; Douglas, supra note 15, at 424 (1980); Craig & Alexander, Wrongful Death in Aviation and the Admiralty: Problems of Federalism, Tempests and Teapots, 37 J. Air. L. & Comm. 3, 9-10 & nn. 24-28 (1971). The few warranted exceptions could be articulated in the proposal's legislative history.

25/ This approach would also be subject to the limited qualifications noted in note 24 supra.

Cf. To Amend Title 28, United States Code, Federal Court Procedures with Respect to Aviation Activity: Oversight Hearing Before the Subcomm. on Administrative Law and Governmental Relations of the House Comm. on the Judiciary, 98th Cong., 1st Sess. 77 (1983) (suggested stipulation of jurisdiction-selecting rule for air disaster cases, such as law of the place of departure).

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of the considerations that support the transfer of actions to a district in a particular state -- such as the occurrence of the event on which the action is based in the state, or a concentration of parties' domiciles in the state -- also tend to support the application of the law of that state.

III. H.R. 3691 -- Increasing the Jurisdictional Amount and Providing for Abstention in Certain Cases

H.R. 3691 incorporates two distinct reform proposals -- it would raise the amount-in-controversy requirement from \$10,000 to \$100,000, and it would provide for abstention in favor of state proceedings under certain circumstances.

The Amount-in-Controversy Requirement. There is no reason in principle why diversity cases involving larger liabilities should not be heard in state court. However, raising the jurisdictional amount is one means of reducing the volume of diversity cases in the federal courts which may be less strongly resisted than the complete abolition approach. H.R. 3691's proposal for raising the amount to \$100,000 would be a step in the right direction. 26/

The Subcommittee should consider some additional measures that would enhance the effectiveness of this type of reform:

The proposed figure of \$100,000 may appear to set a high threshold, but it does not actually do so, since plaintiffs' attorneys commonly allege damages which are many times greater than any recovery that can realistically be expected. Raising the jurisdictional amount to \$100,000 would not even have the effect of excluding completely the class of cases in which damages below \$100,000 are now claimed, since in the presence of a higher jurisdictional threshold some claims would be inflated so as to exceed this threshold.

26/ The amount in controversy requirement for diversity cases has been raised a number of times in the past. It was initially set at \$500 by the First Judiciary Act in 1789. It was raised to \$2,000 in 1887, to \$3,000 in 1911, and to \$10,000 in 1958.

The Consumer Price Index tables prepared by the Bureau of Labor Statistics of the Department of Labor show that 10,000 1958 dollars would be worth about \$35,000 today as a result of inflation. Raising the jurisdictional amount to \$35,000 would accordingly do no more than conform 28 U.S.C. §1331 to Congress's judgment concerning the proper amount at the time of its enactment. The figure of \$3,000 set in 1911 would similarly be equivalent to about \$32,500 today as a result of inflation.

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There is not, at present, any meaningful deterrent to this type of inflation of claims. Dismissal of a facially adequate claim for failure to satisfy the jurisdictional amount requirement depends on a "legal certainty" test that is rarely satisfied. ^{27/} Section 1331(b) of the Judicial Code provides that costs may be denied to and imposed on the plaintiff if the jurisdictional amount is not ultimately recovered, but this sanction has been undermined by narrowing construction ^{28/} and "costs" in the pertinent sense are limited to the narrow range of expenses described in section 1920 of the Judicial Code.

The Subcommittee might consider two modifications of the bill in response to these problems. First, the new jurisdictional amount could be set at some higher figure than \$100,000, such as \$250,000 or \$1,000,000. Second, the sanction of section 1331(b) could be strengthened by making it mandatory whenever the jurisdictional amount is not in fact recovered and by providing a definition of "costs" that more fully captures the true cost to the government of carrying out the adjudication of a diversity case. Broader notions of "costs" of this type are discussed in section VI of this report.

Abstention. H.R. 3691 also provides for staying a diversity case in favor of a state adjudication if certain conditions are satisfied. If a federal district court found that a state court had jurisdiction of all claims and parties, and that the state court could dispose of the claims in a timely manner, a two year stay of the federal proceedings would be required. If the action had not been concluded in the state court within the two-year period, the district court would be permitted to resume the federal proceeding, "if the interests of justice would be so served," upon motion of any party.

As the sponsor's statement notes, this approach would be "sensitive to the potential impact on State courts of a sudden shift in cases from Federal to State courts" since "decisions about when and whether to abstain would be made on the local level." ^{29/} Since some of the opposition to diversity reform reflects concerns over its effect on particular state systems, approaches that permit local variation are worth exploring as the basis for a possible compromise or accommodation. The specific approach proposed in H.R. 3691 does, however, present some problems or concerns.

^{27/} See Wright, Miller & Cooper, Federal Practice and Procedure: Jurisdiction § 3702 (1976).

^{28/} See id. at 402.

^{29/} 129 Cong. Rec. H6023 (July 29, 1983).

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The maximum stay of federal proceedings required by the bill is two years; if the case had not been disposed of in state court within that time, the federal proceeding could resume. The disposition time for a case is not, however, independent of the choices of the parties. In most cases it depends primarily on how long it takes the parties to decide to settle and to reach agreement on the terms of settlement. Even in tried cases the duration of the litigation may depend to a large extent on the decisions of the parties, including the inclination of a party to resort to the familiar tactics of delay. The system proposed in the bill would give a party who preferred a federal forum an incentive to stall in the state proceedings so that the two-year period would elapse and continuation of the federal proceeding could be sought.

The proposal also presents the potential for arbitrary discrepancies in the treatment of different cases and litigants. Resumption of the federal proceeding after two years would not be mandatory, but would depend on the district court's judgment that taking back the case would serve the interests of justice. The "interests of justice" language provides no real guidance, so the decision to resume federal proceedings might largely depend, as a practical matter, on how busy the responsible district judge is with other cases, what his general attitude is towards diversity cases, and how interesting he finds the particular case. A similar potential for arbitrariness is presented by the bill's conditioning of abstention on a district judge's judgment that the action can be disposed of in state court "in a timely manner."

The Subcommittee may wish to consider other approaches that would permit variations responsive to local conditions but would not involve comparable risks of manipulation or arbitrariness. One possibility would be to authorize the judicial councils of the circuits to adopt rules governing abstention in diversity cases for the districts in their circuits, subject to a final coordinating authority in the Judicial Conference. This would permit the adoption of rules suited to the conditions in particular districts, and would provide coordinating mechanisms at both the circuit level and the national level which would be capable of addressing problems of forum-shopping and other difficulties that might otherwise result from the application of different abstention rules in different courts. 30/ The suggested approach

30/ In this respect the suggested approach avoids a problem with the proposal of Professor David Shapiro that the individual district courts be allowed to decide whether to retain diversity jurisdiction. See Shapiro, Federal Diversity Jurisdiction: A Survey and a Proposal, 91 Harv. L. Rev. 317, 339-55 (1977). It is also preferable in that it commits the
(Footnote Continued)

may be compared to that of Title III of H.R. 6872 of the 97th Congress, which would permit the circuit councils to adopt expediting or priority rules for civil cases, subject to a coordinating authority in the Judicial Conference. 31/

IV. H.R. 3692 -- An Increase in the Jurisdictional Amount and Compulsory Arbitration

H.R. 3692 would raise the amount-in-controversy requirement for diversity cases to \$100,000 and would require that diversity cases be submitted to arbitration. The arbitration would be carried out pursuant to rules issued by the Judicial Conference, and would normally have to be completed within a year. Trial de novo could be obtained following arbitration, but if the party seeking a trial obtained a substantially less favorable result from the judgment of the court than from the arbitration, that party would be required to pay the opposing party the full expense of the litigation, including attorney's fees. 32/

Our remarks concerning the proposal in H.R. 3691 to raise the jurisdictional amount to \$100,000 are equally applicable to the corresponding proposal in this bill. The arbitration proposal raises both questions of design and questions of basic approach:

Questions of Design. The bill contains few specifications concerning the arbitration system, leaving most matters to be decided by the Judicial Conference. This approach makes the actual operation of the system unpredictable to some extent. It does, however, have the practical advantage of avoiding the need to reach agreement on the details of the system at the legislative stage. It would also make adjustments in the system in light of experience with its operation easier to implement than an approach in which significant changes would normally require new legislation.

(Footnote Continued)

decision to bodies -- the circuit councils and the Judicial Conference -- which include both circuit and district judges. Since the intake of diversity cases at the district court level has a large effect on the workload of the courts of appeals, see note 54 infra, it is appropriate to have circuit judges as well as district judges involved in such a decision.

31/ See H.R. Rep. No. 824, 97th Cong., 2d Sess. 17 (1982).

32/ For purposes of valuating fees and expenses, the bill incorporates by reference the provisions of the Equal Access to Justice Act.

The bill provides that the limitation period applicable to an action would generally be suspended while arbitration was going on, but would start to run again when the arbitration was completed or one year after the start of the arbitration, whichever was earlier. This is problematic in a case in which the arbitration continues beyond a year because of unnecessary delay by the defendant. The limitation period would begin to run again against the plaintiff, who might be forced to choose between seeking trial de novo despite the fact that the arbitration was still going on, or foregoing the possibility of trial de novo as a result of the expiration of the limitation period.

An amendment is needed to ensure that a party would not be prejudiced or forced to make an undesired choice on account of delay attributable to the other party. The bill is obviously correct in suspending the general limitation period applicable to an action when it is submitted to arbitration, but restarting such a period subsequently would not be necessary if the arbitration rules specified suitable time limits for completing arbitration and seeking trial de novo. 33/

The bill provides for fee-shifting against a party who seeks trial de novo if the result of the trial is substantially less favorable than the arbitral award. Under current law, there are a broad variety of rules and statutes which require that other remedies be pursued before a federal judicial forum is sought. 34/

33/ Restarting a statutory limitation period after a certain time is not, in any event, an effective means of controlling delay during arbitration or after it, since many years may remain prior to the expiration of such a period. Delay by either party could be effectively controlled through the Judicial Conference's prescription of time limits for completion of the various stages of arbitration and for seeking trial de novo following the conclusion of arbitration. The rules of the three federal district courts that have utilized arbitration do include such time limits and provide that the arbitral decision becomes final if trial de novo is not sought within the time allowed. See E.A. Lind & J.E. Shapard, Evaluation of Court-Annexed Arbitration in Three Federal District Courts 99-118 (Federal Judicial Center 1983).

34/ For example, under the Federal Tort Claims Act, a claim must first be presented to the responsible agency. See 28 U.S.C. § 2675. Employment discrimination claims must be presented to the EEOC for conciliation as provided in 42 U.S.C. § 2000e-5. State judicial remedies must be exhausted before a state prisoner can apply for federal habeas corpus. See 28 U.S.C. § 2254(b). Under the Civil Rights of

(Footnote Continued)

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There are also many provisions that require a party who has proceeded to litigation without necessity or adequate justification to bear the resulting costs and expenses, where "necessity" and "justification" are either the subject of an express judicial determination or are defined in terms of the outcome of the case. ^{35/} In the circumstances in which H.R. 3692 authorizes fee-shifting -- a substantially less favorable verdict than the arbitral award -- the outcome of the litigation demonstrates that proceeding to trial was not necessary to secure the compensation to which the party who sought a trial was entitled, since he would actually have done better if he had accepted the arbitral award. Requiring that party to bear the other party's expenses in such circumstances is similar in principle to the existing cost and fee-shifting provisions noted above.

While we see no problem in principle with this provision, the conditioning of fee-shifting on a "substantially less favorable" outcome introduces an element of vagueness -- and an

(Footnote Continued)

Institutionalized Persons Act, suits by prisoners under 42 U.S.C. § 1983 may be stayed up to 90 days while the plaintiff pursues state administrative remedies conforming to federal standards. See 42 U.S.C. § 1997e.

^{35/} For example, "costs," as defined in 28 U.S.C. § 1920, are normally included in a judgment against a party in a federal case. Costs may be shifted to the plaintiff in a diversity case if he fails to recover the jurisdictional amount. See 28 U.S.C. § 1332(b). Under 28 U.S.C. § 1912 an appellate court "may adjudge to the prevailing party just damages for his delay, and single or double costs" when a judgment is affirmed on appeal.

There are dozens of rules and statutes that authorize awards of attorney's fees, either generally or under certain conditions. For example, attorney's fees may be awarded in any case against a party who proceeds in bad faith. The Equal Access to Justice Act makes the government liable for attorney's fees to prevailing parties in civil actions not sounding in tort, unless the government's position is substantially justified or certain other exceptions apply. See 28 U.S.C. § 2412. Under 42 U.S.C. § 1983 and the other statutes specified in 42 U.S.C. § 1988, a prevailing plaintiff is normally awarded attorney's fees and a prevailing defendant is awarded attorney's fees if the suit was frivolous, harassing, or vexatious. 42 U.S.C. § 2000e-5(k) generally authorizes awards of attorney's fees to prevailing parties in employment discrimination cases. 28 U.S.C. § 1875(d)(2) authorizes fee-shifting in favor of a juror who successfully sues an employer for discrimination based on jury service.

attendant likelihood of interpretive litigation -- which serves no obvious purpose. If the outcome of the trial is the same as the arbitral award or less favorable than the arbitral award to any degree, it appears that the recourse to litigation was unnecessary to secure the compensation to which the party who sought a trial was entitled, and the basic rationale for fee-shifting is applicable. It would be preferable to provide for fee-shifting whenever the outcome of the trial is not more favorable than the arbitral award, rather than when it is "substantially less favorable." 36/

Questions of Basic Approach. The more basic question for the Subcommittee to consider is whether requiring arbitration for all diversity cases in all parts of the country is too large a step to take at one time. The available evidence concerning the effects of arbitration consists of experiments in three federal districts which have gone on for a number of years, 37/ and a larger body of experience with arbitration in state systems. 38/ If a uniform arbitration requirement seems excessive at this time, the Subcommittee may wish to consider a more flexible approach under which the circuit councils would be given authority to require arbitration of diversity cases in the districts in their circuits, subject to a coordinating authority in the Judicial Conference. 39/ This would enable the workload resulting from diversity cases to be reduced in districts in which arbitration proved to be productive, and would provide a larger body of experience that would inform future legislative decisions concerning the use of arbitration in federal cases.

V. H.R. 3693 -- Limiting Access to a Federal Forum to Out-of-State Litigants

The final bill in the series is a classical intermediate reform option which was proposed by the American Law

36/ Two federal district courts have used a "not more favorable" standard in their arbitration rules concerning cost-shifting as a sanction for unnecessary resort to trial. See E.A. Lind & J.E. Shapard, supra note 33, at 111, 118.

37/ See generally id.; Levin, Court-Annexed Arbitration, 16 U. Mich. J.L. Reform 537 (1983).

38/ See generally Levin, supra note 37.

39/ As noted earlier, see text accompanying note 31 supra, this is similar to the approach proposed for civil priority rules in H.R. 6872.

Institute 40/ and considered in the 95th Congress. 41/ It would limit filing in federal court in diversity cases to out-of-state litigants. In relation to the historical justification of diversity jurisdiction as a means of protecting parties from bias against persons from other states, there is no point in allowing a federal forum to be sought by an in-state litigant. Such a litigant could only benefit from local favoritism or partiality in state proceedings.

In relation to current law, H.R. 3693 would simply equalize the position of plaintiffs and defendants. Section 1441(b) of the Judicial Code now bars a defendant from removing a diversity case to federal court if he is sued in his home state, but a plaintiff is free to initiate a diversity suit in federal court in his home state.

The reform of H.R. 3693 would not reduce the federal diversity caseload by a proportion fully equal to the current proportion of cases brought into federal court by in-state litigants. Consider, for example, a case that under the current system would be brought in federal court by an in-state plaintiff. Under the reform the plaintiff would instead have to initiate the suit in state court, if he wished to litigate in his own state. This does not necessarily mean, however, that the litigation would be carried out in state court, since the defendant would retain the option of removing the case to federal court. Also, a plaintiff with the capacity to litigate in more than one state might deliberately choose to sue in some state other than his home state in order to have access to a federal forum. 42/ It is, nevertheless, reasonable to expect that the reduction in federal

40/ See American Law Institute, Study of the Division of Jurisdiction Between State and Federal Courts 123-25 (1969).

41/ See generally 1978 Senate Diversity Jurisdiction Hearings, supra note 2; 1977 House Diversity Jurisdiction Hearings, supra note 2.

42/ This possibility would be limited, however, by the difficulty of litigating out-of-state for many litigants, and by venue restrictions. Under the amendment to 28 U.S.C. § 1391(a) proposed in the bill, venue would be limited to districts in which all plaintiffs or all defendants reside, and districts containing a substantial part of the events giving rise to the claim or a substantial part of the property that is the subject of the action.

The potential for such forum-shopping could be further limited by confining access to a federal forum to cases in which at least one of the parties is litigating in his home state, as proposed in the ensuing textual discussion.

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diversity cases resulting from the enactment of H.R. 3693 would be substantial.

We would recommend one improvement in the proposal -- the bill should provide that the party adverse to the party seeking a federal forum must be a citizen of the state in which the suit is brought. In the absence of such a limitation, a federal forum could be obtained where neither party was a citizen of the state in which the suit was brought. ^{43/} There is no point in retaining this option under the historical justification of diversity jurisdiction noted above, ^{44/} since bias against persons from other states in the forum state would not create a relative advantage for either party in a case in which both parties were not citizens of the forum state.

VI. Other Reform Options

A. Discretionary Appellate Review

The Subcommittee should consider a suggestion of Judge Carl McGowan of the D.C. Circuit that appellate review in diversity cases be made available only by leave of the courts of appeals. ^{45/} Diversity cases now account for about 15% of appeals from district court decisions; making appellate review discretionary would plausibly eliminate much of the burden that is currently imposed on the courts of appeals by these cases.

This reform would involve a departure from the normal rule that a litigant is afforded one appeal as a matter of right beyond the trial stage. However, the principal benefits provided by appellate review in other contexts -- correction of legal errors and maintenance of decisional uniformity -- are not realized in the normal manner in diversity cases.

Federal diversity jurisdiction, to begin with, involves transferring a class of state law cases from the state judges -- who have the greatest expertise and familiarity with this body of law -- to federal district judges, whose exposure to state law is more limited. The federal courts of appeals are further removed from the state systems whose law they are required to apply in diversity cases. A federal district judge often has had prior

^{43/} This was not allowed between 1789 and 1875. Changes in the statutory language in 1875 abrogated the requirement that at least one party must be a citizen of the forum state.

^{44/} I.e., protection from bias against persons from other states.

^{45/} See McGowan, The View from an Inferior Court, 19 San Diego L. Rev. 659, 666 (1982).

experience as a practitioner in the legal system of the state in which his district is located. The federal appellate circuits, however, generally extend over a number of states, so a circuit judge hearing a diversity appeal will most likely have no first-hand experience with the legal system of the state whose law is being applied in the case.

Diversity appeals accordingly subject the decisions of district judges, who have some degree of expertise on state law matters, to review for error by circuit judges, who have relatively little expertise in pertinent state law. Appellate review of this character is less likely to provide significant benefits in terms of increased accuracy than appellate review in normal federal cases which depend on the interpretation and application of federal law. 46/

Appellate review in diversity cases also does not operate in the normal manner to produce decisional uniformity. The federal courts of appeals have no authority to expound or develop state law, but are limited to serving as "ventriloquist's dummies" for the state courts in diversity cases; their decisions on state law issues do not, of course, have any binding effect on the courts of the states within the circuit. Moreover, a federal appellate decision on a state law issue has only provisional value in producing uniformity in the decisions of the district courts in later diversity cases in the circuit, since it loses effect if the state courts subsequently address the issue and reach a different conclusion. 47/

Hence, appellate review in federal diversity cases serves the normal functions of appellate review, at best, to a limited degree. It is dubious that the slight benefits that may result from making such review available as a matter of right justify the costs and burdens that result to the federal courts of

46/ In other words, if an appellate panel reverses a district court judgment on federal law grounds, it is probable that the appellate panel is correct and the district court was mistaken. When an appellate panel reverses a district court judgment on state law grounds in a diversity case, however, it may be equally probable or more probable that the appellate panel is mistaken and the district judge was correct. If this is so, then appellate review of state law questions in diversity cases produces no net gain in terms of error correction, or may actually be counterproductive.

47/ See American Institute of Chemical Engineers v. Reber-Friel Co., 682 F.2d 382, 392 (2d Cir. 1982) (Feinberg, C.J., concurring).

appeals. For diversity cases that incidentally present significant questions of federal law or procedure, discretionary review by the courts of appeals should be an adequate recourse. 48/

B. Charging a User's Fee

Federal diversity jurisdiction has remained in existence because many members of the trial bar and certain of their clients prefer maintaining a choice of forums in diversity cases. Gratifying this preference consumes a large part of the total resources of the federal judicial system. This misallocation of federal resources could be corrected by charging diversity litigants who seek a federal forum the costs to the federal government of carrying out the resulting adjudications. This would preserve a federal forum in diversity cases for litigants who considered such a forum valuable enough to warrant paying for it, but would end the commitment of federal resources to a function which the states are fully competent to perform.

Costs can now be charged to litigants in diversity cases and other cases in federal court, but the expenses characterized as "costs" are a small fraction of the true expense of adjudications to the federal government. They do not include, for example, the portion of the salary of the judge and judicial support personnel allocated to work on a case, or the costs of maintaining courtroom facilities and other elements of overhead. A fuller measure of costs would be required in implementing this approach.

One possibility would be to determine on a case-by-case basis how much carrying out an adjudication had cost the government, and to charge that amount to the party who had filed in federal court. The determinations involved would be similar in many respects to those required in making awards of attorney's fees. While the example of attorney's fees awards suggests that this approach would not be impossible, it also suggests that it could be burdensome and time-consuming. A case-by-case determination would also increase record-keeping burdens, since

48/ Under this proposal it would not, of course, be necessary for each judge of a court of appeals to pass on an application for discretionary review. The courts of appeals would be free to adopt the more efficient procedure of delegating the screening function for discretionary review to a smaller number of judges, just as the function of deciding cases on the merits is now routinely delegated to three-judge panels. Cf. Fed. R. App. P. 22 (request to a circuit court for a certificate of probable cause, which is required as a prerequisite to appeal in habeas corpus proceedings, is to be considered by a circuit judge or judges as the court directs).

judicial personnel would have to keep track of the amount of time they had spent on particular diversity cases.

A second possibility would be to have diversity litigants as a class bear the full cost of diversity cases as a class by charging in each case the average amount. In other words, the average total cost to the federal judicial system of a diversity case would be determined, and any diversity litigant filing in federal court would be charged a filing fee equal to that amount. This would be the simplest and most efficient approach.

A final possibility would be some hybrid of the preceding two approaches. For example, a uniform fee corresponding to the basic salary and overhead costs of the average diversity case might be charged in each case, and, in addition, readily ascertainable costs of specified types which had been present in a particular case could be charged at their actual amounts.^{49/} This approach would avoid a potentially burdensome case-by-case inquiry as to the actual total cost of a case to the system, but would result in a closer approximation of the amount charged to actual cost.

C. Requiring a Particularized Showing of Bias

The continuation of diversity jurisdiction is sometimes justified by reference to a supposed danger of bias in state proceedings against litigants from other states. Access to a federal forum in diversity cases might be conditioned on a showing that bias of this type would actually be encountered in state proceedings.

This approach would be consistent with that taken under other remedies for bias. In both the state and federal systems, for example, a purely abstract possibility of bias is not grounds for granting a change of venue; rather, an actual danger of bias in the initial venue must be established. Under the "local bias" rationale for retaining federal diversity jurisdiction, it is conceived of as a change-of-venue mechanism, by which cases are removed from a state jurisdiction to the federal jurisdiction as a response to possible bias against out-of-state litigants.

Given this conception, it is difficult to see why the showing of an actual danger of bias that is normally required for change of venue should be dispensed with. This approach could be implemented by requiring, as a condition for proceeding in federal court in diversity cases, a showing by a party that he would be denied an impartial trier or tribunal in state proceedings on account of bias against persons from other states,

^{49/} Cf. the compensation schedules for "costs" in chapter 123 of the Judicial Code.

and that transferring the case to federal court would avoid such bias.

D. Redefining Corporate Citizenship

A final possibility would be to re-define the notion of state citizenship for corporations so that diversity of citizenship would be present in a smaller class of cases. This has been done in the past. State citizenship for corporations was initially defined as the state of incorporation. As a result of legislation adopted in 1958, however, a corporation is now also deemed a citizen of the state in which it has its principal place of business. ^{50/} Since most diversity cases involve corporate litigants, ^{51/} broadening the notion of state citizenship for corporations could have a significant effect on the volume of diversity cases.

It might, for example, be provided that a corporation is a citizen of any state in which it is licensed to do business. ^{52/} This approach seems consonant with the supposed function of diversity jurisdiction as a safeguard against bias against out-of-state parties. Under the stated condition, a corporation would be an in-state enterprise as well as an out-of-state enterprise -- even if its principal place of business and place of incorporation were elsewhere -- and would not obviously be more exposed to the possibility of local bias than other business operations in the state. ^{53/}

^{50/} See 28 U.S.C. § 1332(c). As a result of legislation adopted in 1964, § 1332(c) further provides that, in a direct action against an insurer, the insurer is also deemed a citizen of the state of which the insured is a citizen.

^{51/} See 1978 Senate Diversity Jurisdiction Hearings, supra note 2, at 66 (one or both of the opposing parties is a corporation in over 75% of diversity cases).

^{52/} For discussion of other possible changes in the notion of corporate citizenship, see American Law Institute, supra note 40, at 125-29; Wright, Miller & Cooper, supra note 27, §3601 at 583 (proposal to bar federal forum where corporation doing business in state is sued on a claim arising from its activities in the state).

^{53/} Consider, for example, a case in which a citizen of Delaware sues a corporation which is incorporated in Delaware ("Corporation A") but does no business there, and an otherwise similar case in which a Delaware citizen sues a corporation ("Corporation B") which is not a citizen of Delaware as that notion is currently defined but which

(Footnote Continued)

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In sum, the Department of Justice supports the general abolition of diversity jurisdiction proposed in H.R. 3689 and supports the intermediate reform options proposed or suggested by the remaining bills as discussed in this report.

The limitation or elimination of diversity jurisdiction is long overdue. No other pending reform is of comparable importance in relieving the overload of the federal judicial system ^{54/}; no reform could be more appropriate as an adjustment of federal-state responsibilities under the principles of federalism. We commend the leadership you have shown on this issue and earnestly hope that this initiative will be met with a spirit of statesmanship and accommodation among other interested members of Congress.

The Office of Management and Budget has advised that there is no objection to the submission of this report from the standpoint of the Administration's program.

Sincerely,

Robert A. McConnell
Assistant Attorney General

(Footnote Continued)

carries on substantial business in Delaware and employs many people in the state. If we assume -- as the "local bias" rationale for retaining diversity jurisdiction requires -- that people in Delaware are prejudiced against out-of-state businesses, it is apparent that Corporation A would be at greater risk on account of such prejudice than Corporation B, but the current rules would allow a federal forum in the suit against B but not A. The suggested re-definition of corporate citizenship would avoid such perverse results.

54/ As noted earlier, diversity cases account for about one-quarter of all civil filings, 40% of all civil trials, and 60% of all civil jury trials in the federal districts courts, and for about 15% of appeals from district court decisions. They take up over one-fifth of the total work time of federal district judges. See Federal Judicial Center, Federal District Court Time Study 15 (1979).